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NOTES AND COMMENTS

Bills and Notes—Garnishment—Check as Assignment

In a recent federal¹ case the holder for value of certain checks was not allowed a preferred claim as against a creditor of the drawer who garnished the deposit before presentment. The court held that a check of itself did not work as an assignment of the deposit and that there were not sufficient facts outside of the actual drawing and delivery of the checks to constitute one, although the drawer made a deposit the next day, seemingly to cover the checks. The drawer was a cotton broker; the checks were issued to purchase cotton; and the deposit garnished was largely, if not entirely, made up from the proceeds of the re-sale of the cotton.

Before the Uniform Negotiable Instruments Law a minority of the courts held that a check of itself constituted an assignment,² but the majority ruled otherwise.³ Some cases held that even though the check was no assignment as against the drawee, it was as between the drawer and holder.⁴ North Carolina was of this class according to *Hawes v. Blackwell*.⁵

Section 189 of the N. I. L.⁶ incorporated the majority view, although for a short time after passage of the statute a few courts took the posi-

¹ Marx v. Maddrey, 106 F. Supp. 535 (E. D. N. C. 1952).

² Munn v. Burch, 25 Ill. 35 (1860) (leading case); Rogers v. Durant, 140 U. S. 298 (1890); Industrial Trust v. Weakley, 103 Ala. 458, 15 So. 854 (1894); Commonwealth v. Kentucky Distilleries, 132 Ky. 521, 116 S. W. 766 (1909); Whitehouse v. Whitehouse, 90 Me. 468, 38 Atl. 374 (1897). See citations collected in 7 AM. JUR., BANKS § 532, p. 384 (1937); NORTON, BILLS AND NOTES 584 (4th ed. 1914); 2 MORSE, BANKS AND BANKING § 494 n. 1 (6th ed. 1928). Munn v. Burch, *supra*, referred to check as assignment and/or contract for the benefit of payee. Under this minority view the holder was preferred to the garnishing creditor. Dillman v. Carlen, 105 Wis. 14, 80 N. W. 932 (1899).

³ National Bank v. Millard, 10 Wall. 152 (U. S. 1870) (leading case); Exchange Bank v. Sutton Bank, 78 Md. 577, 28 Atl. 563 (1894); Gramel v. Carmer, 55 Mich. 201, 21 N. W. 418 (1884). For extensive collection of citations see 2 MORSE, BANKS AND BANKING § 493 n. 1 (6th ed. 1928); NORTON, BILLS AND NOTES 584, 585 (4th ed. 1914).

⁴ Moore v. Lowery, 25 Iowa 336 (1868); Nat. Exchange Bank v. McLoon, 73 Me. 498 (1882); Coates v. First Nat. Bank, 91 N. Y. 20 (1883). See citations in 2 MORSE, BANKS AND BANKING § 495 n. 1 (6th ed. 1928). Mr. Morse is violently opposed to the old majority rule and that of the N. I. L.

⁵ 107 N. C. 196, 12 S. E. 245 (1890). This decision held that a check, although no assignment as between drawee and payee, was an equitable assignment *pro tanto* as between drawer and payee or holder as soon as drawn and delivered.

⁶ N. C. Gen. Stat. § 25-197 (1943). "A check of itself does not operate as an assignment of any part of the funds to the credit of the drawer with the bank, and the bank is not liable to the holder unless and until it accepts or certifies the check." (Italics added.)

tion that it was intended to protect only the drawee bank.⁷ Thus in *McClain and Norvet v. Torkelson*⁸ the Iowa court held that the holder of a check acquired a right to the drawn-on deposit superior to that of a garnishing creditor. However, this holding has been expressly overruled in Iowa.⁹ The clear weight of authority now supports the view that under the N. I. L. a check, *of itself*, does not have the character of an assignment, not only as between the holder and drawee, but also as between the holder and drawer;¹⁰ an attaching creditor is preferred to the holder,¹¹ unless all of the circumstances surrounding the writing of the check are such that the court can declare it an equitable assignment or can otherwise find exceptions to the provisions of the N. I. L.¹²

Where there has been a deposit for the specific purpose of meeting a check, or class of checks, with clear notice or directions to the bank that the deposit is to be held for this end, some courts have ruled that the bank holds the deposit in trust,¹³ others that there is a specific deposit and that therefore the restrictions of the N. I. L. concerning a check *of itself* would not apply and the holder would have a right against the bank.¹⁴ The Supreme Court of North Carolina has held that in such a case there is a trust, and the depositor has a preference to the amount of the check as against receivers of the insolvent bank and may recover for the use of the holder.¹⁵ The court has stated as dictum that the

⁷ *Farrington v. Flemming*, 94 Neb. 108, 142 N. W. 297 (1913); *Elgin v. Gross-Kelly*, 20 N. M. 450, 150 Pac. 922 (1915); *Glennan v. Rochester Trust*, 209 N. Y. 12, 102 N. E. 537 (1913); *Federal Reserve Bank v. Peters*, 139 Va. 45, 123 S. E. 379 (1924); *Raesser v. Nat. Exchange Bank*, 112 Wis. 591, 88 N. W. 618 (1902).

⁸ 187 Iowa 202, 174 N. W. 42 (1919).

⁹ *Leach v. Mechanics Savings Bank*, 202 Iowa 899, 211 N. W. 506 (1926).

¹⁰ *Kaesemeyer v. Smith*, 22 Idaho 1, 123 Pac. 943 (1912); *Leach v. Mechanics Savings Bank*, 202 Iowa 899, 211 N. W. 506 (1926); *Perry v. Bank of Smithfield*, 131 N. C. 117, 42 S. E. 551 (1902). See 7 AM. JUR., BANKS § 534, pp. 396, 7 (1937).

¹¹ *Fulton v. Gesterding*, 47 Fla. 150, 36 So. 56 (1904); *Kaesemeyer v. Smith*, 22 Idaho 1, 123 Pac. 943 (1912); *Boswell v. Citizens Savings Bank*, 123 Ky. 485, 96 S. W. 797 (1906); *Livestock State Bank v. Hise*, 150 Minn. 301, 185 N. W. 498 (1921); *Wileman v. King*, 120 Miss. 392, 82 So. 265 (1919); *Jones v. Crumpler*, 119 Va. 143, 89 S. E. 232 (1916).

¹² *First Nat. Bank v. Propp*, 198 Iowa 809, 200 N. W. 428 (1924); *Dolph v. Cross*, 153 Iowa 289, 133 N. W. 669 (1911); *Slaughter v. First Nat. Bank*, 18 S. W. 2d 754 (Tex. 1929); *Hatley v. West Texas Bank*, 284 S. W. 540 (Tex. 1926). See Comment, 37 YALE L. J. 626 (1928); Notes, 5 A. L. R. 1667 (1920), 50 A. L. R. 403 (1927).

¹³ *Eshbach v. Byers*, 164 Ill. App. 449 (1911); *Foss v. Hume*, 130 Me. 32, 153 Atl. 181 (1931); *Corporation Commission v. Merchants Bank & Trust Co.*, 194 N. C. 125, 138 S. E. 530 (1927); *Morton v. Woolery*, 48 N. D. 1132, 189 N. W. 232 (1922); *Straus v. Tradesmens Nat. Bank*, 36 Hun 451 (N. Y. 1885); *Payne Bros. v. Burnett*, 151 Tenn. 496, 269 S. W. 27 (1925); *Cotulla State Bank v. Herron*, 191 S. W. 154 (Tex. Civ. App. 1917); *cf. Walker Co. v. Alden*, 6 F. Supp. 262 (E. D. Ill. 1934) (with extensive list of citations p. 264 n. 1). *But cf. Andrew v. Waterville Savings Bank*, 205 Iowa 888, 219 N. W. 52 (1928).

¹⁴ *Decatour Creamery v. West Side Bank*, 213 Ill. App. 220 (1919); *First Nat. Bank v. Barger*, 115 S. W. 726 (Ky. 1909); *Hitt Fireworks v. Scandinavian Am. Bank*, 114 Wash. 167, 195 Pac. 13 (1922).

¹⁵ *Corporation Commission v. Merchants Bank & Trust Co.*, 194 N. C. 125, 138

cestui que trust may recover in equity.¹⁶ But in *General American Life Insurance Co. v. Stadiem*,¹⁷ where the holder sought recovery, the court did not apply the trust theory, although the drawer had deposited \$21.38 for the specific and sole purpose of meeting the check for \$21.38 and had instructed the agents and employees of the bank that the deposit was to be held for that sole purpose. The decision stated only that a holder of an unaccepted check has no action against the bank.¹⁸

Where there is an oral promise to the drawer from the bank that certain checks will be paid, the courts have often allowed the holder recovery against the bank on the theory that he is beneficiary of a contract for the benefit of a third party.¹⁹ The North Carolina court refused to apply this theory in *Brantley v. Collie*.²⁰ Although a valid contract between the drawer and the drawee for the benefit of the payee was conceded, the court held that such a contract gave the payee no action against the bank.²¹ The court apparently decided that the N. I. L. did not allow the payee of an unaccepted check rights against the bank no matter what the circumstances surrounding the issuance of the check.

S. E. 530 (1927). The case leads a collection of authorities in Note, 57 A. L. R. 386 (1927). See also Notes, 10 N. C. L. Rev. 381 (1932), 13 N. C. L. Rev. 209 (1935).

¹⁶ *Corporation Commission v. Merchants Bank & Trust Co.*, 193 N. C. 696, 700, 138 S. E. 22, 24 (1927). This is based on the doctrine set out in *Morton v. Woolery*, 48 N. D. 1132, 189 N. W. 232 (1922). See note 13 *supra*.

¹⁷ 223 N. C. 49, 25 S. E. 2d 202 (1943).

¹⁸ The court relies for authority on the rule (now uniform) in *Cincinnati H. & D. R. R. v. Metropolitan Nat. Bank*, 54 Ohio St. 60 (1896) that a check of *itself* is no assignment of drawer's funds in drawee bank, and that the bank is not liable to the holder until acceptance. This rule should not be controlling, if indeed it is at all applicable, here where we have circumstances outside of the check itself to consider. The court did not mention specific deposit.

¹⁹ *Ballard v. Home Nat. Bank*, 91 Kan. 91, 136 Pac. 935 (1913) is the case most cited for this doctrine, although it is not clear that the court did not base its decision on equitable assignment. The drawer was a livestock dealer. The bank agreed he could draw checks on it to buy livestock, provided he would deposit the re-sale proceeds in time to cover the checks. The bank applied these deposits to a pre-existing debt of the drawer. The payee of one of these checks sued the bank and recovered. The court ruled that the holder recovered on the basis of the entire transaction, rather than the promise alone. It was not required that the payee know of the contract for his benefit. In *Saylors v. State Bank*, 99 Kan. 515, 163 Pac. 454 (1917) the facts were almost the same, except that the bank got 8% interest on the resale proceeds and \$3 per car-load of livestock bought and sold. It was held that the payee, as beneficiary of the agreement, could recover from the bank. See also *Goeken v. Bank*, 100 Kan. 177, 163 Pac. 636 (1917), *connected case*, 104 Kan. 370, 179 Pac. 321 (1919); *Singer v. Citizens Bank*, 79 Okla. 267, 193 Pac. 41 (1920); *Webster v. First State Bank*, 46 S. D. 460, 193 N. W. 675 (1923). These cases were applications of the third party beneficiary doctrine announced in *Lawrence v. Fox*, 20 N. Y. 268 (1859).

²⁰ 205 N. C. 229, 171 S. E. 88 (1933).

²¹ The court distinguished the *Ballard* and *Saylors* cases, note 20 *supra*, saying that there the bank was interested in the livestock purchased by the drawer from the holder. Though there was specified consideration of extra commission to the bank in the *Saylors* case, the bank appears to have had no greater interest in the *Ballard* case or most of the other cases decided on the same theory than did the bank in the instant case. See Comment, 46 YALE L. J. 483 (1937). The distinction does not seem a real one.

In either of the situations previously discussed, or where there is a combination of the two,²² courts have sometimes labeled the legal result an "equitable assignment."²³ This term is also applied to the relationship of rights that results from an understanding, express or implied, between the drawer and payee which shows an intent to assign the debt of the drawee bank (the deposit).²⁴ However, this is only an assignment as between drawer and payee and does not necessarily give the holder a right against the bank unless the bank is a mere stakeholder and has had notice of the agreement.²⁵

Even if a court allows a holder a right against the bank or its receivers, it is not settled whether he will be preferred to a garnishing creditor. *Dolph v. Cross*²⁶ held that since the drawee could not apply

²² The combination seems to be the most common situation. *First Nat. Bank v. Prikett*, 19 Ala. App. 204, 95 So. 920 (1923) (specific deposit); *Wilson v. Dawson*, 52 Ind. 513 (1876) (must use for specific purpose); *Moravek v. First Nat. Bank*, 119 Kan. 84, 237 Pac. 921 (1925) (bank cannot appropriate deposit to its own claim); *Joy v. Grasse*, 173 Minn. 289, 217 N. W. 365 (1927); *York v. Farmers Bank*, 105 Mo. App. 127, 79 S. W. 968 (1904) (privity between bank and holder); *Central Coal & Coke v. State Bank*, 226 Mo. App. 594, 44 S. W. 2d 188 (1931) (bank's carrying account in general ledger mere matter of bookkeeping); *Paige v. Springfield Nat. Bank*, 12 Ohio App. 196 (1919) (specific deposit, cannot use to pay other checks); *Re Warren's Bank*, 209 Wis. 121, 244 N. W. 594 (1932) (bank held agent of depositor, had no title).

These cases (this footnote and note 20 *supra*) almost all arise out of agreements to finance agricultural marketing. They are generally referred to as "The Livestock Cases." See Comment, 46 YALE L. J. 483 (1937).

²³ *Few v. First Nat. Bank*, 40 Ga. App. 791, 151 S. E. 456 (1930) (specific deposit); *Manget v. Nat. City Bank*, 168 Ga. 876, 149 S. E. 213 (1929) (specific deposit); *Guaranty State Bank v. Summer*, 278 S. W. 459 (Tex. Civ. App. 1925) (specific deposit and agreement); *Boyle v. Vivian State Bank*, 55 S. D. 441, 226 N. W. 579 (1929) *semble*; *Ballard v. Home Nat. Bank*, 91 Kan. 91, 136 Pac. 935 (1913) *semble*.

²⁴ *Fourth Street Nat. Bank v. Yardley*, 165 U. S. 634 (1897) (leading case). Here the drawer, having insufficient funds to settle a clearing house debt, told payee that it had \$25,000 on deposit with its New York correspondent, the drawee, showing a statement in proof. The court held this sufficient for an equitable assignment *pro tanto*, so payee was entitled to a preference as against receiver of the drawer, which had gone insolvent. *Dunlap v. Commercial Bank*, 50 Cal. 476, 195 Pac. 688 (1920); *First Nat. Bank v. O'Byrne*, 117 Ill. App. 473 (1913); *Hove v. Stanhope Bank*, 138 Iowa 39, 115 N. W. 476 (1908); *First Nat. Bank v. Rogers-Admundson-Flynn*, 151 Minn. 243, 186 N. W. 575 (1922); *Merchants Nat. Bank v. State Bank*, 172 Minn. 24, 214 N. W. 750 (1927); *Muller v. King*, 209 N. Y. 239, 103 N. E. 138 (1913); *Boyle v. Vivian State Bank*, 55 S. D. 441, 226 N. W. 579 (1929); *Austin v. Public Nat. Bank*, 2 S. W. 2d 463 (Tex 1928).

²⁵ In *Fourth Street Nat. Bank v. Yardley*, 165 U. S. 634 (1897) the court held that it is an equitable assignment *pro tanto* as against the drawer, any mere volunteers, and persons charged with notice. In *First Nat. Bank v. Rogers-Admundson-Flynn*, 151 Minn. 243, 186 N. W. 575 (1922) it was held that there was an assignment as between drawer and payee and payee was allowed recovery against drawee who had ample notice of the assignment. In *Merchants Nat. Bank v. State Bank*, 172 Minn. 24, 28, 214 N. W. 750, 752 (1927) the court states that "as between drawer and payee the check (in question) operates as an equitable assignment, and, after receiving notice of the intention and purpose of the parties, the bank must comply with the directions of the drawer, if it can do so without prejudice to its own rights . . ."

²⁶ 153 Iowa 289, 133 N. W. 669 (1911); *cf.* *First Nat. Bank v. Propp*, 198 Iowa 809, 200 N. W. 428 (1924) (specific deposit). *Contra*: *Mayer v. Chattahoochee Bank*, 51 Ga. 325 (1874).

a specific deposit to its own claim against the drawer, creditors garnishing the deposit would be excluded as they could rise no higher than the bank itself were it a creditor.²⁷ If it is decided that the facts constitute an equitable assignment, then it is probable the holder, as "owner" of part of the deposit, will be preferred to garnishing creditors before presentment, even though there has been no notice to the bank before the garnishment proceedings.²⁸ In the recent case of *Lipe v. Bank*,²⁹ the North Carolina court held there was an assignment as between the depositor and his assignee, and title passed without notice to the debtor bank. But no check was involved, and there was an express assignment. Whether the court would apply this reasoning where the facts attending the drawing and delivery of a check showed an intent to assign is yet to be seen.

The non-assignment rule of the N. I. L. has resulted in many injustices to check holders, not only in the cases of the bank's insolvency or garnishment of the drawer's account, but also where the drawer dies or himself goes insolvent before presentment.³⁰ Most courts have recognized this and have tried to qualify the N. I. L. whenever the facts allow, but the law on this point is confused since the situations naturally overlap and the courts are not precise in the use of theories they employ. However, the North Carolina court seems to regard it as good policy to protect the drawee bank at all costs. Otherwise it is difficult to explain why it did not apply the trust theory in the *Stadium* case or the third party beneficiary theory in the *Brantley* case. The court seems to take the position that the N. I. L. precludes their considering special circum-

²⁷ Where the court holds a trust, in theory the garnishing creditor would again be excluded since the garnishee bank would no longer be the debtor of the depositor. But a court might not be willing to extend the trust theory this far.

²⁸ A great majority of the courts hold that an assignment of the debt, before garnishment proceedings, even where no notice is given to the debtor before the garnishment, gives a preference to the assignee. *Walters & Walker v. Whitlock*, 9 Fla. 89 (1860); *Walton v. Horkan*, 112 Ga. 814, 38 S. E. 105 (1901); *McDowell v. Hopfield*, 148 Md. 84, 128 Atl. 742 (1925); *Schoolfield v. Hirsh*, 71 Miss. 55, 14 So. 528 (1893); *Market Nat. Bank v. Raspberry*, 34 Okla. 243, 124 Pac. 758 (1912). Intervention in the garnishment proceedings is all the notice necessary. *Hall v. Kansas City Terra Cotta Co.*, 97 Kan. 103, 154 Pac. 210 (1916). In *Slaughter v. First Nat. Bank*, 18 S. W. 2d 754 (Tex. 1929) there was a clear agreement between the drawer and payee that proceeds of the re-sale of the live-stock (paid for with the check in question) would be deposited with the drawee to meet the check. The court held that the check, when given under such circumstances, was an equitable assignment of the amount of the deposit necessary to meet it. Hence payee had rights to the deposit superior to those of a garnishing creditor. The court also held that notice of the agreement to the bank was unnecessary since the decision was based on equitable assignment and not on deposit for a specific purpose.

²⁹ 236 N. C. 328, 72 S. E. 2d 759 (1952).

³⁰ This should be particularly apparent in North Carolina, where a tobacco grower, for instance, could lose the proceeds of a large part or even all of his year's crop. See excellent discussion of the injustices and inequities of the non-assignment rule in Comment, 60 YALE L. J. 1007 (1951); also Feezer, *Death of a Drawer of a Check*, 14 MINN. L. REV. 124 (1929).

stances outside the actual drawing and delivery of a check, apparently attaching no significance whatever to the words "check of itself" in the statute.³¹ The new Uniform Commercial Code has dealt directly with this problem and, if adopted in North Carolina, will expressly overrule this position of the court.³² It does not appear that a case has arisen in this state wherein a holder sought preference over a garnishing creditor where the surrounding facts show an intent to appropriate the deposit to the payment of the outstanding check. When such a case is presented, it is hoped the court will be less reluctant to allow the action since the drawee bank would be actually a mere stakeholder.

J. ALLEN ADAMS, JR.

Criminal Law—Suspension of Sentence

Although early decisions of the North Carolina Supreme Court held the suspended sentence illegal,¹ in 1894 the Court gave its complete approval to this type of judgment.² Subsequent decisions have held that the power to suspend the imposition (the pronouncing of the terms of punishment) or execution (the putting into effect of the punishment as pronounced) of sentence in a criminal case is within the inherent powers of a court.³ In addition, the use of the suspended sentence has been ex-

³¹ See note 6 *supra*. Notes, 6 N. C. L. REV. 325 (1928) and 8 N. C. L. REV. 201 (1930) take the same attitude.

³² UNIFORM COMMERCIAL CODE § 3-409 (Official Draft 1952).

"DRAFT NOT AN ASSIGNMENT.

(1) A check or other draft does not of itself operate as an assignment of any funds in the hands of the drawee available for its payment, and the drawee is not liable on the instrument until he accepts it.

(2) Nothing in this section shall affect any liability in contract, tort or otherwise arising from any letter of credit or other obligation or representation which is not an acceptance."

The comment states:

"1. . . . The assignment may, however, appear from other facts, and particularly from other agreements, express or implied; and when the intent to assign is clear the check may be the means by which the assignment is effected."

"2. The language of the original section 189 that the drawee is not liable 'to the holder,' is changed as inaccurate and not intended. . . ."

"3. Subsection (2) is new. It is intended to make it clear that this section does not in any way affect any liability which may arise apart from the instrument itself. The drawee who fails to accept may be liable . . . to the holder for breach of the terms . . . of any . . . agreement by which he is obligated to accept. He may be liable in tort or upon any other basis because of his representation that he has accepted, or that he intends to accept. The section leaves unaffected any liability of any kind apart from the instrument."

It is understood that this new act has been introduced for the first time, in the current session of the Massachusetts Legislature.

¹ State v. Hatley, 110 N. C. 522, 14 S. E. 751 (1892); State v. Bennett, 20 N. C. 170 (1838).

² State v. Crook, 115 N. C. 760, 20 S. E. 513 (1894). See Coates, *Punishment for Crime in North Carolina*, 17 N. C. L. REV. 205, 215 (1939); *A Survey of of Statutory Changes in North Carolina in 1937*, 15 N. C. L. REV. 345 (1937).

³ The phraseology most often used by our court is "inherent power . . . to suspend judgment or stay execution." State v. Gibson, 233 N. C. 691, 698, 65 S. E. 2d 508, 513 (1951); State v. Stallings, 234 N. C. 265, 66 S. E. 2d 822 (1951);